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IN THE

Supreme Court of the United States

October Term, 1935

Nos. 184-186

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, *Petitioner*,

v.

JOHN J. WATTS.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, *Petitioner*,

v.

HUGH C. SICARD.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, *Petitioner*,

v.

PARKER SLOANE.

BRIEF FOR RESPONDENTS IN OPPOSITION ON PETITIONS FOR WRITS OF CERTIORARI TO THE CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

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August 17, 1935.

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BRIEF FOR RESPONDENTS IN OPPOSITION ON PETITIONS FOR WRITS OF CERTIORARI TO THE CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

[Italics and bracketed matter in quotations ours unless otherwise noted.]

Opinions Below.

The opinion of the Board of Tax Appeals (R. 58) is reported in 28 B. T. A. 1056. The opinion of the Circuit Court of Appeals is reported in 75 F. (2d) 981.

Jurisdiction.

The judgments of the Circuit Court of Appeals, were entered on March 11, 1935. A petition for rehearing was denied on March 27, 1935. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925.

Questions Presented.

The Government has not in our view correctly stated the questions in the case. They are:

1. Does a transaction by which the taxpayers "exchanged all of the stock of Alloys [Corporation] solely for stock in Vanadium [Corporation] and bonds of Alloys"* constitute the "acquisition by one corporation of at least a majority of the voting stock and at least a majority of the total number of shares of all other classes of stock of another corporation"? Such acquisition is a type of transaction which the term "reorganization" is defined by Section 203 (h) (1) (A) of the Revenue Act of 1924 to include. Or is the dissolution of Alloys an additional factor indispensable if the transaction is to qualify as a reorganization?

The Court below held that the transaction did constitute a reorganization within the quoted definition, dissolution not being necessary.

2. If in a reorganization the taxpayer receives stock and mortgage bonds in exchange for all of a corporation's stock, has he, in so far as the mortgage bonds are concerned, received "stock or securities"?

Section 203 (b) (2) of the Revenue Act of 1924 provides that no gain or loss is to be recognized in "stock or se-

* Quoting from the "single sentence" with which the Circuit Court of Appeals said the "controlling facts" might be stated (R. 182).

curities" received in exchange for "stock or securities" in a reorganization. The Government asserts that an exchange of stock for stock and mortgage bonds is not, to the extent that mortgage bonds are received, an exchange for "stock or securities", and consequently that the mortgage bonds, even if not the stock, should be treated as "gain". This contention was made for the first time in a petition for rehearing in the Court below. The petition was denied without opinion.

Statement.

The facts are stated in the opinion of the Court below and in the Government's petition. A relevant fact, not there stated, is that Mr. Sloane, one of the taxpayers, became a member of the Board of Directors and of the Executive Committee of Vanadium Corporation as part of the transaction (R. 130).

The decision that there was here a "reorganization" as defined by Section 203 (h) (1) (A), notwithstanding that Alloys was not dissolved, is in complete harmony with the language of this Court in *Pinellas Ice & Cold Storage Co.* v. *Commissioner*, 287 U. S. 462, which nowhere suggests, much less decides, that dissolution is required. The decision here moreover follows an administrative construction deliberately sanctioned by Congress. Despite contrary statements in the petition its opinion shows that the Court below gave full consideration to the obvious fact that the transaction in this case did partake of the nature of a merger or consolidation.

In the Court below the Government contended that because the Alloys Corporation had not been dissolved the

transaction here at issue failed to constitute a "reorganization" within the statutory definition. Such had been the holding of the Board of Tax Appeals. That issue the Court below considered and decided.

In its petition here the Government fails to emphasize the lack of dissolution, but instead asserts that the Court below did not give heed to the broad principle of the decision of this Court in *Pinellas Ice & Cold Storage Co.* v. *Commissioner*, 287 U. S. 462, that to qualify as a "reorganization" the transaction must bear "real semblance to a merger or a consolidation", and must "partake of the nature of a merger or a consolidation", phrases used by this Court in its opinion in the *Pinellas* case.

This presentation is misleading. No such question was presented to the Court below. Parties and counsel assumed that the principle of the *Pinellas* case was controlling. It would have indeed been strange had any other assumption been made especially as the broad principle adopted in the construction of the statute by this Court in the *Pinellas* case had already been advanced by the Circuit Court of Appeals of the Second Circuit in *Cortland Specialty Co.* v. *Commissioner*, 60 F. ((2d) 937, a case cited and approved by this Court in the *Pinellas* case.

Although the Circuit Court of Appeals did not set out to determine whether the transaction bore "real semblance to a merger or consolidation" *in haec verba* it did consider at length the effect of failure to dissolve the corporation the stock of which was acquired—the only respect in which the Board of Tax Appeals had found, and the Government claimed, that the transaction failed to constitute a "reorganization" within the statutory definition.

The *Pinellas* case did not make, "Was there semblance to a merger or consolidation?" words of art to which every court must address itself. The Court below necessarily

held in effect that there was semblance to a merger or a consolidation here.

A brief examination of the *Pinellas* case will show that there is no inconsistency between that decision and this.

The Act of 1924, Section 203 (h), at issue here, provides:

> "As used in this section and sections 201 and 204—
>
> (1) The term 'reorganization' means (A) a merger or consolidation (including the acquisition by one corporation of at least a majority of the voting stock and at least a majority of the total number of shares of all other classes of stock of another corporation, or substantially all the properties of another corporation) • • •."

This Court said of similar provisions in the 1926 Act in the *Pinellas* case (at 287 U. S. 469-470):

> "The words within the parenthesis may not be disregarded. *They expand the meaning of 'merger' or 'consolidation' so as to include some things which partake of the nature of a merger or consolidation but are beyond the ordinary and commonly accepted meaning of these words*—so as to embrace circumstances difficult to delimit but which in strictness cannot be designated as either merger or consolidation."

It seems too clear for argument that by these words this Court intended simply to characterize the type of transactions described by the words in parenthesis as "partak(ing) of the nature of a merger or consolidation". The Court adverted to the obvious fact that:

> "the acquisition by one corporation of at least a majority of the voting stock and at least a majority of the total number of shares of all other classes of stock of another corporation"

intrinsically does "partake of the nature of a merger or consolidation", as does the acquisition of *all* of another corporation's stock in the instant case; it did not intend to require that there be some unstated additional factor, such as dissolution in order that the transaction might qualify as a "reorganization".

The true basis of the Court's decision in the *Pinellas* case was not (h) (1) (A) of Section 203. This Court commented on the words in parenthesis in (h) (1) (A) to correct a misconstruction of that clause by the lower Court in that case, saying "if passed without comment may produce perplexity" (287 U. S. 469). The statute actually controlling in the *Pinellas* case was Section 203 (b) (3) in the 1926 Act, as follows:

> "No gain or loss shall be recognized if a corporation a party to a reorganization exchanges property, in pursuance of the plan of reorganization solely for stock or securities * * *."

In the *Pinellas* case the taxpayer had received short term notes. This Court said (at 287 U. S. 468-469):

> "These notes—mere evidence of obligation to pay the purchase price—*were not securities within the intendment of the act* and were properly regarded as the equivalent of cash * * *. In substance the petitioner sold for the equivalent of cash; *the gain must be recognized.*"

The Court proceeded to make the comment on Section 203 (h) (1) (A) quoted on the preceding page of this brief and continued (at 287 U. S. 470):

> "But the mere purchase for money of the assets of one Company by another is beyond the evident

> purpose of the provision, and has no real semblance to a merger or consolidation. Certainly, we think that to be within the exemption the seller must acquire an interest in the affairs of the purchasing company more definite than that incident to ownership of its short-term purchase-money notes."

The Court then approved the opinion in *Cortland Specialty Co.* v. *Commissioner*, 60 F. (2d) 937, 939, 940, There the Court had said (at p. 940):

> "The very reason that Section 203 (e)* requires that some of the property received in exchange should be '*stock or securities*' [italics by the Court] is to deprive a mere sale for cash of the benefits of an exemption and to require an amalgamation of the existing interests * * * The word 'securities' was used so as not to defeat the exemption in cases where the interest of the transferor was carried over to the new corporation in some form".

These quotations show that the *Pinellas* case turned on the requirement that property received in exchange must be "stock or securities". The Court not only failed to require that there be some additional factor, such as dissolution, in connection with an acquisition, but it explicitly condemned the holding of the lower court in that case that there must be a "merger or a consolidation" in the "ordinary and commonly accepted meaning of those words" (287 U. S. 470).

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* Meaning the 1926 Act which also ruled in the *Pinellas* case. A similar provision is in the 1924 Act which rules in the instant case.

The Court below has followed an administrative construction deliberately sanctioned by Congress in the reenactment of the statute.

The statute is not ambiguous. The Court below demonstrates that its decision follows a continuous administrative construction of many years which has thereby become embodied in the law. *United States* v. *Dakota-Montana Oil Co.*, 288 U. S. 459, 466-467; *Helvering* v. *Bliss*, 293 U. S. 144, 151.

There Is No Conflict Between Circuits.

The Government asserts that the decision of the Circuit Court of Appeals in the instant case conflicts with various decisions by other Circuit Courts of Appeals. The basis of the alleged conflict is what the Government regards as the failure of the Court below to give effect to the doctrine of the *Pinellas* case. If the Court below has given effect to that doctrine, there is, therefore, no conflict even on the Government's own statement.

There is no conceivable difference between the Circuits as to the principle to be applied in these cases—the alleged "conflicts" relate to the application of a principle accepted by all to diverse and individual facts. As the doctrine of the *Pinellas* case found precedent in the decision of the Second Circuit Court of Appeals in the *Cortland Specialty* case, specifically approved and followed by this Court in the *Pinellas* case, it can hardly be argued the Court below does not recognize that doctrine.

Four cases are cited as conflicting. In the *Prairie* case the Court held that a sale of property for cash did not meet the definition of reorganization in Section 203 (h) (1) (A).

It was obviously not an exchange of stock for "stock or securities" (Section 203 [b] [2]) as in the instant case (*Prairie Oil & Gas Co.* v. *Motter*, 66 F. [2d] 309 [C. C. A. 10]). In the *Von Weise* case, the Court found that all of the common stock, but not a majority of all other classes of stock, had been acquired so that the acquisition did not effect a reorganization within the terms of Section 203 (h) (1) (A) (*Von Weise* v. *Commissioner*, 69 F. [2d] 439 [C. C. A. 8th]). In the *Nelson* case, the Court held that cash and non-voting preferred stock, received in exchange for property, did not effect a reorganization, for it did not provide the recipient with the requisite "interest in the affairs of purchasing company" (*John A. Nelson Co.* v. *Commissioner*, 75 F. [2d] 696 [C. C. A. 7th]). In the *G. & K.* case, the Court held there was no merger or consolidation and that "substantially all" the properties of a corporation had not been acquired (Section 203 [h] [1] [A]) because the corporation had been left with substantial assets (*G. & K. Mfg. Co.* v. *Commissioner*, 76 F. [2d] 454 [C. C. A. 4th]). In none of these cases was it held that dissolution of the absorbed corporation was prerequisite to a "reorganization". Not only the principle but the result of these cases is in every sense consistent with the decision here.

Stock and Mortgage Bonds Are "Stock or Securities".

The Government urges that the transaction here at issue be unscrambled and the bonds, even if not the stock, be taxed as not being "securities" within Section 203 (b) (2). The decision of the Second Circuit Court of Appeals in

Worcester Salt Co. v. *Commissioner*, 75 F. (2d) 251, is urged as authority for that procedure. The Court nowhere in its opinion in the *Worcester Salt* case holds that bonds are not "securities"; it concluded on the complex and special facts of that case that the transaction amounted to a purchase. As the *Worcester Salt* case was decided two weeks before the instant case by the same Court, as Judges MANTON and A. N. HAND (the author of the *Cortland Specialty* opinion) participated in both decisions, and as the Court in the instant case denied a petition for rehearing based upon alleged inconsistency with the *Worcester Salt* case, it is abundantly plain that the Court below, at any rate, could find no such inconsistency.

Here the taxpayers, stockholders in Alloys, transferred to Vanadium all of the stock in Alloys for stock in Vanadium and mortgage bonds of Alloys. Unquestionably there was an exchange of stock for "stock or securities" resulting in "interest in the affairs of the purchasing company" (287 U. S. 470—*Pinellas* case) and "amalgamation of the existing interests" (60 F. [2d] 940—*Cortland Specialty* case), an "interest" and "amalgamation" emphasized by Mr. Sloane's becoming a director and a member of the Executive Committee of Vanadium. The strict provisions of the indenture securing the bonds comply fully with the meaning of the word "securities". The property received was precisely what the statute contemplated.

Conclusion.

The statute has already received the authoritative construction of this Court. The Second Circuit Court of Appeals has pronounced no principle, novel, or important, or inconsistent with any decision of this Court. Indeed it was the construction of the statute by the Second Circuit Court of Appeals in the *Cortland Specialty* case that was accepted and approved by this Court in the *Pinellas* case. The dispute here, and the alleged conflict with other circuits, turn only on the application of an accepted principle to highly diverse and specialized factual situations. The application of that principle here by the Court below has the further support of an administrative construction of long standing to approve of which the statute was intentionally designed. The petitions for writs of certiorari should be denied.

Dated, New York, August 17, 1935.

Respectfully submitted,

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RESPONDENTS' BRIEF.

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RESPONDENTS' BRIEF.

(Italics and bracketed matter in quotations ours unless otherwise noted.)

Opinion Below.

The Opinion of the Court below is reported in 75 F. (2), at page 981, and is found at pages 91-95 of the Record. The Opinion of the United States Board of Tax Appeals (R. 28-38) is reported in 28 B. T. A. 1056.

Jurisdiction.

The cases are here on writs of certiorari. Jurisdiction is invoked under Section 240 (a) of the Judicial Code, as amended.

Question Presented.

The question presented is whether or not gain or loss in the transaction described below should be recognized for income tax purposes in the year in which the transaction occurred. The answer depends upon whether or not the transaction was a "Reorganization" within the meaning of Section 203 (h) (1) of the Revenue Act of 1924.

Statement of the Case.

The respondents were all the stockholders of United States Ferro Alloys Corporation, hereinafter called "Alloys" (R. 29). On December 6, 1924, the respondent Sloane, acting for all three, entered into an agreement with Vanadium Corporation of America, hereinafter called "Vanadium" (R. 51, 55). By this agreement Sloane

"does hereby exchange, transfer, and deliver"

to Vanadium 30,000 shares, constituting the total capital stock, of Alloys, and agrees to deliver to Vanadium the resignations of all the officers and directors of Alloys (R. 58). In return, Vanadium

"does hereby exchange, transfer, and deliver"

to Sloane 66,666⅔ [subsequently reduced to 32,103 (R. 54)] shares of Vanadium stock and $1,161,184.50 face amount of bonds of Alloys. These bonds matured, according to their

terms, in substantially equal amounts annually over a period of eight years commencing February 1, 1925, subject to call on ninety days' notice. They were secured by a trust mortgage on Alloys' land, plant and equipment at Niagara Falls and, by the terms of the agreement, the payment of principal and interest was guaranteed by Vanadium (R. 58-59).

Vanadium agreed to repay certain creditors of Alloys $338,815.50 advanced by them on chrome contracts and for unused power (R. 56, 57-58) and assumed the payment of other liabilities of Alloys for materials delivered, labor, expenses, etc., aggregating $255,000 (R. 57). Sloane, one of the respondents, "in consideration of the exchange of the said stock" agreed to become a Director and a member of the Executive Committee of Vanadium (R. 64).

The agreement was duly executed according to its terms (R. 54): Vanadium acquired all the stock of Alloys, giving in exchange shares of its own stock and mortgage bonds of Alloys, and Sloane joined the Board of Directors and the Executive Committee of Vanadium. Vanadium, as agreed, assumed the payment of the aforesaid liabilities of Alloys and made the payments it agreed to make to creditors of Alloys, and thereupon Vanadium became a creditor of Alloys in the amount so paid (R. 51). It was stipulated (R. 54) that these payments were not income to respondents.

In their Income Tax Returns for 1924, respondents treated the foregoing transaction as a Reorganization, the gain or loss on which was postponed for tax purposes by the provisions of Section 203 (b) (2) of the prevailing Revenue Act. The Commissioner, however, proposed to recognize a gain and to assess a tax deficiency against respondents. They filed appeals to the Board of Tax Appeals and the proceedings were consolidated for hearing and decision (R. 28). The Board of Tax